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C O N F I D E N T I A L SECTION 01 OF 03 LAGOS 000061

SIPDIS

STATE FOR AF/W
STATE FOR CA/OCS/FROBINSON
STATE FOR EB/ESC/IEC/ENR/BLEVINE
STATE FOR DS/IP/AF
STAT FOR INR/AA
STATE PASS DOE FOR DAS JBRODMAN AND CGAY
STATE PASS TREASURY FOR ASEVERENS AND SRENENDER
STATE PASS DOC FOR PHUPER
STATE PASS TRANSPORTATION FOR MARAD
STATE PASS OPIC FOR CDUFFY
STATE PASS TDA FOR BTERNET
STATE PASS EXIM FOR JRICHTER
STATE PASS USTR FOR ASST USTR SLISER
STATE PASS USAID FOR GWEYNAND AND SLAWAETZ

E.O. 12958: DECL: 12/27/2014
TAGS: ECON EINV EPET PGOV NI
SUBJECT: LAGOS BUSINESS EXECS GRIM ON NIGERIAN BUSINESS CLIMATE

REF: A. ABUJA 001946

¶B. ABUJA 02040
¶C. LAGOS 02447

Classified By: Classified By: Acting Consul General Ronald Kramer for R easons 1.4 (D & E)

¶1. (C) Commercial and Energy Officers recently met with group of senior business executives from American firms based in Lagos, who expressed substantial concern with the Nigerian business environment and import bans. They believe the GON is failing to develop the institutions and policies needed to promote growth in the private sector. The Exxon Mobil Managing Director noted the GON is not even funding oil projects at a sufficient level to maintain current production capacity of approximately 2.4 million barrels/day. The Texaco MD predicted the labor dispute over fuel prices would become an issue again in January, when authority for the fuel price reduction expires. The Citibank MD expressed concern, given that politicians are already jockeying to position themselves for the 2007 election, with how the GON will spend the $16 billion in reserves accumulated due to record high oil prices. End Summary.

Serious Concern about Trade and Business Environment
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¶2. (C) Commercial and Energy Officers recently met with group of senior business executives from American firms based in Lagos. They groused about the Nigerian business environment and import bans. There was general agreement that the GON's economic 'dream team' is a well-educated but relatively powerless group. (Reftel B) There was a consensus that President Obasanjo instead seems susceptible to a small coterie of political insiders and businessmen who use nationalist economic rhetoric to justify import bans and trade restrictive practices that promoted the group's narrow self-interest. Discussants noted that there is a plan to phase out the import bans by 2007, but also remarked on a failed promise to do so two years ago.

Personal Connections Needed where Institutions Fail
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¶3. (C) The Commercial Officer reported on the recent TIFA negotiation in Abuja, noting the prepared statements by USTR, DOS and USDA were quite critical of the GON. The business executives were disappointed but not surprised that GON interlocutors did not view the import bans and other trade restrictions as negative. There was general alarm at the situation suffered by Proctor and Gamble, which had to temporarily shut down its new Lagos diaper factory in September due to an import ban that blocked raw material essential to diaper-marking from coming into Nigeria. Despite successful operations in difficult markets around the world, Proctor and Gamble apparently has not able to break even after thirteen years of operation in Nigeria. (Reftel A) Discussants noted that while Finance Minster Okonjo-Iweala appears to have intervened to resolve Proctor and Gamble's specific issue, the GON is failing to develop the institutions and policies to promote a functioning private sector. Instead, problems continue to be addressed through informal methods and personal relationships.

EM Foresees Production Decline at Current Funding Levels
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¶4. (C) Exxon Mobil Managing Director John Chaplain stated that joint venture (JV) projects with the parastatal Nigerian National Petroleum Corporation had been funded at $4.23 billion for the year, with Exxon Mobil's funding requests cut by one-third (Reftel C). Chaplain assessed that gas projects had been funded sufficiently, but not oil projects. (Note: This shift likely reflects the GON's strategic move towards exploitation of Nigeria's ample gas reserves, estimated to be the 7th largest in the world. End note.) Chaplain expressed serious concern the GON is not funding oil projects at a level sufficient to maintain current production capacity of approximately 2.4 million barrels/day. If oil production declines, Chaplain noted that government revenues will also decline, as currently about 70 percent of GON revenues are derived from oil production. Discussants noted a decline in oil revenues would have serious fiscal implications for Nigeria. Chaplain observed that the GON appears to be deliberately starving oil projects of revenue; he believes the GON is attempting to force energy firms to accept alternative funding arrangements, where the firms are paid in oil or through other financial arrangements, rather than through their share of the revenue stream generated by JV projects.

Authority for Fuel Subsidy Runs Out in January
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¶5. (C) Jules Harvey, Vice President and Managing Director of Texaco Nigeria (Chevron Texaco's downstream subsidiary) predicted the dispute over fuel prices would remain mute until January, when temporary authorization for subsidies allowing for lower consumer fuel prices runs out.

Refinery Privatization Pace May Accelerate
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¶6. (SBU) On the issue of refinery privatization, Harvey noted that Credit Suisse First Boston had been commissioned to manage the refinery privatizations, but the Bureau of Public Enterprises had apparently never paid the firm. After the temporary departure of the consultants carrying out the work, NNPC has now agreed to pay the CSFB bill. He anticipates new developments in refinery privatizations as soon as the consultants return to Nigeria. (Comment: Mission anticipates that absent full deregulation of the downstream fuel sector, the GON will continue to experience serious difficulties in attracting credible foreign investors to rehabilitate existing refineries or to build new ones.)

Concern over Bill Mandating Local Refining
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¶7. (C) Harvey explained that energy firms remain concerned about legislation which may force them to refine a set percentage of their crude oil locally. (Note: The four domestic refineries currently run at about 20 percent of capacity. As Nigeria currently lacks sufficient domestic refining capacity to implement this bill, many in the industry view this measure as a backdoor attempt to force the majors to construct a domestic refining industry in Nigeria. The majors have strenuously resisted prior attempts to force them to carry out refining in Nigeria. In various past showdowns with the majors, the GON has threatened them with loss of production rights; the majors have countered that they would halt production if forced to refine domestically. The GON has then backed off. If successful deregulation of the downstream market is carried out, Mission believes the majors would entertain refining some products locally. Industry members are also concerned such a bill would force them to sell a percentage of their products domestically, when the Nigerian fuel market remains regulated and prices below actual international values.

$13 Billion in Reserves;Where will the Money be Spent?
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¶8. (C) Harvey remarked that due to high international oil prices in excess of budget assumptions, Nigeria increased its foreign reserves from around $2 billion 16 months ago, to over $13 billion today. Harvey noted the GON budget was based on benchmark assumptions of monthly oil production of 2.7 million barrels/day at $27/barrel. While there has been no final decision on the allocation of these excess funds above the benchmark price, the GON plans to use them for an unspecified combination of building a 'rainy day' fund, paying off international debt, and financing infrastructure improvements. A low benchmark also allows the GON to avoid boom and bust budgetary cycles that have plagued past Nigerian governments. The 2.7 million barrels/day production benchmark, while well above Nigeria's current 2.4 million barrels/day capacity, appears to take into account production anticipated to come on-line in 2005 at Shell's Bonga and Exxon Mobil's Yoho fields. Khaled Qurashi, Managing Director of Citibank, noted that while the GON says it plans to spend excess oil revenues on infrastructure and debt reduction, there has not yet been any meaningful drawdown of these

reserves, despite the GON's many overdue bills with its contractors. Qurashi expressed concern that, in the run-up to the 2007 elections, this money might be spent on poorly conceived projects or diverted for election spending. He also noted that the perception of Nigeria having a large surplus fund might also argue against some countries considering debt relief for Nigeria.

## Need for an American Business Association?

¶9. (C) There was a consensus among the discussants that the Nigerian-American Chamber of Commerce is not performing its proper role of a bi-national chamber, in terms of business and free trade advocacy. Discussants noted several current Chamber members had spoken out in favor of import bans, as their personal businesses benefited from these trade barriers. With the growing complexity of U.S. and Nigerian business and trade relations, discussants agreed there is a need a vehicle to genuinely fulfill the role of a bi-national Chamber of Commerce. While not wanting to alienate the current Chamber, discussants agreed that the establishment of a new organization is worth exploring.

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